



KANSAS

DIVISION OF THE BUDGET
DUANE A. GOOSSEN, DIRECTOR

KATHLEEN SEBELIUS, GOVERNOR

November 4, 2004

To: Governor Kathleen Sebelius, and the Legislative Budget Committee

From: The Kansas Division of the Budget and the Kansas Legislative Research Department

Re: State General Fund Receipts for FY 2005 (Revised) and FY 2006

Estimates for the State General Fund are developed using a consensus process that involves the Division of the Budget, the Legislative Research Department, the Department of Revenue, and three consulting economists from state universities. This estimate is the base from which the Governor and the Legislature build the annual budget. The Consensus Group met on November 3, 2004, to revise the FY 2005 estimate and to develop the first estimate for FY 2006.

For FY 2005, the estimate was increased by \$89.2 million, or 2.0 percent, above the previous estimate (made in April and subsequently adjusted for legislation). The overall revised SGF estimate of \$4.631 billion is 2.5 percent above actual FY 2004 receipts. The initial estimate for FY 2006 is \$4.841 billion, which is \$210.0 million, or 4.5 percent, above the newly revised FY 2005 figure. The FY 2006 estimate does not subtract any demand transfers converted to revenue transfers, while the FY 2005 estimate subtracts \$71.8 million in demand transfers that were converted to revenue transfers. If transfers are treated in a similar fashion in both years, the FY 2006 growth would be \$138.2 million, or 2.9 percent.

Detailed information regarding the specific sources of revenue constituting total receipts is presented in Table 1. Table 2 compares the FY 2005 estimate developed last spring with the recently revised estimate. Table 3 compares the revised FY 2005 estimate to the FY 2006 estimate.

Economic Forecast for Kansas

The Kansas economy is expected to continue the trend of subdued, but positive growth through calendar year 2006. Several key factors that affected the consensus estimates include high energy prices; cautious, but increased capital investments by businesses; a lower unemployment rate; an improved agricultural sector; and dampening retail sales.

The national economy is expected to grow at a slower pace over the next two years. Nominal Gross Domestic Product (GDP) is expected to grow by 6.6 percent in 2004; 5.6 percent in 2005; and by 4.8 percent in 2006, while real GDP is expected to grow by 4.4 percent, 3.7 percent, and 3.0 percent, respectively. U.S. personal income also is expected to increase. The growth is anticipated to be 5.3 percent in 2004; 5.0 percent in 2005; and 5.2 in 2006. A listing of the key economic indicators is shown in the following table:

Key Economic Indicators

	2003	2004	2005	2006
Consumer Price Index for All Urban Consumers	2.3 %	2.7 %	2.1 %	2.1 %
Real U.S. Gross Domestic Product	3.0	4.4	3.7	3.0
Nominal U.S. Gross Domestic Product	4.9	6.6	5.6	4.8
Nominal U.S. Personal Income	3.2	5.3	5.0	5.2
Corporate Profits before Taxes	15.0	15.5	38.0	4.0
Nominal Kansas Gross State Product	4.5	5.8	4.8	4.4
Nominal Kansas Personal Income:				
Dollars in millions	\$80,466	\$84,300	\$88,400	\$92,706
Percentage Change		4.8 %	4.9 %	4.9 %
Nominal Kansas Disposable Income:				
Dollars in millions	\$72,451	\$75,500	\$78,500	\$81,500
Percentage Change		4.2 %	4.0 %	3.8 %
Interest Rate for State General Fund (based on fiscal year)	1.63	1.19	2.13	3.09
Kansas Unemployment Rate (based on fiscal year)	5.3	5.1	5.9	5.7

Inflation Rate

In 2003, the rate of inflation, as measured by the Consumer Price Index for All Urban Consumers (CPI-U), was 2.3 percent. The inflation rate in 2004 is expected to be higher at 2.7 percent. The rate is anticipated to drop back to 2.1 percent in 2005 and remain at that level through 2006.

Kansas Personal Income

Kansas Personal Income (KPI) is expected to grow by 4.8 percent in 2004 above 2003. The growth rate is expected to increase to 4.9 percent in 2005 and remain at that level through 2006.

Interest Rates

The Pooled Money Investment Board is authorized to make investments in US Treasury and agency securities; highly rated commercial paper; and repurchase agreements and certificates of deposit of Kansas banks. In FY 2003, the state earned 1.63 percent on its State General Fund portfolio. The average rate of return forecasted for FY 2004 is 1.19 percent. For FY 2005, the forecasted rate is 2.12 percent and 3.09 percent for FY 2006.

Employment

Labor market statistics indicate that unemployment in Kansas is up, but experts believe that the employment outlook generally is improving. The statewide unemployment rate for FY 2003 was 5.3 percent and is expected to drop to 5.1 percent in FY 2004. The latest statistics indicate that Kansas unemployment is still below the national rate of 5.4 percent (September 2004). The overall Kansas unemployment rate for FY 2005 is expected to be 5.9 percent before decreasing to 5.7 percent in FY 2006.

The Kansas Department of Labor stated that the US Department of Labor will be making a significant change to its methodology in 2005. The Kansas Department of Labor anticipates that the change in the way that the unemployment rate is calculated will translate into a higher unemployment rate. Adjustments will be made back to 2000, when the last decennial census was conducted. Experts believe that the unemployment rate will increase by 1.0 percent because of the U.S. Department of Labor's adjustments.

Agriculture

Net farm income in Kansas increased 451.0 percent from \$251.9 million to \$1,386.9 million in 2003. For this same period, the national net farm income increased by 59.0 percent.

The All Farm Products Index of Prices received by Kansas farmers was 105 in September, compared with 112 a year ago. The monthly average prices farmers received for wheat, corn, sorghum, and soybeans were above year ago levels for the first six months of 2003, then began to fall behind year ago prices as it became obvious that row crop production would be excellent. Using current forecasts for 2004 production and the projected prices released by the USDA in October, the value of production for the four major crops in Kansas likely will be down 5.0 to 10.0 percent from last year's levels. Cattle marketings through September are running 2.1

percent below last year, but prices remain well below last year's levels. Hog prices have been above last year's levels.

Oil and Gas

The average price per taxable barrel of Kansas crude oil is estimated to be \$40 in FY 2005 and to decrease to \$33 in FY 2006. Gross oil production in Kansas is expected to continue to remain steady at 34.0 million barrels throughout the forecast period (FY 2005 and FY 2006).

The price of natural gas is expected to increase from the FY 2004 level of \$4.17 per mcf to \$5.50 per mcf in FY 2005 and then to \$5.00 per mcf in FY 2006. Natural gas production in FY 2004 was 417.6 million cubic feet. Production is expected to continue to decline for the foreseeable future as natural gas reserves, especially those in the Hugoton field, are depleted. The forecast is for 385.0 million cubic feet in FY 2005 and 355.0 million cubic feet in FY 2006.

State General Fund Receipts Estimates

Each individual SGF source was reevaluated independently and consideration was given to revised and updated economic forecasts, and year-to-date receipts. Additional information was provided by the Department of Revenue, the Insurance Department, the State Treasurer's Office, the Pooled Money Investment Board, and the Kansas Department of Labor.

Tax Receipts

FY 2005. Estimated tax receipts for FY 2005 were increased by \$89.2 million. Individual income tax receipts account for \$60.1 million of the total increase, while severance tax receipts account for \$27.8 million. Corporation income tax receipts also were increased by \$22.0 million. One factor supporting the increase in the individual income tax estimate is that FY 2004 receipts from this source exceeded the final estimate by more than \$58.0 million. Data show that the average balance due increased by \$60 per check over the prior year. In addition, withholding receipts have shown significant growth in the first four months of FY 2005.

Increases to the severance tax are attributable to higher than anticipated energy costs. The war in Iraq, unrest in the Middle East, and the effects of hurricanes in the Gulf of Mexico have caused price increases in both oil and natural gas. Corporation income tax receipts were increased because of the current economic expansion in business investment. This trend is expected to continue through the forecast period.

The retail sales tax estimate was reduced for FY 2005 from \$1,670.9 million to \$1,650.0 million (-\$20.9 million). This reduction was based on slower than expected consumer spending through the first four months of the fiscal year and the expectation that the pattern will continue throughout the rest of the fiscal year.

Alternatively, the compensating use tax estimate was increased by \$8.7 million from \$224.3 million to \$233.0 million. This tax source estimate was affected by an apparent increase in business purchases.

Other tax source estimates that were increased include motor carrier property tax; estate tax; tobacco products tax; liquor enforcement; and corporate franchise taxes. Motor carrier receipts were increased by \$1.5 million because there are more carriers and operating units that were valued for tax year 2004.

The estate tax estimate was increased by \$1.0 million from \$49.0 million to \$50.0 million. Statutory changes also were made to the corporate franchise tax during the 2004 Legislative Session. Beginning January 1, 2005, collection of the corporate franchise tax will be transferred from the Secretary of State's Office to the Department of Revenue. This tax is assessed against businesses on the basis of \$1.25 per each \$1,000 of net worth. The Secretary of State's Office will continue to collect the corporate franchise fee, which is assessed to all businesses and non-profit organizations. The overall estimate for both sources was increased because the collections for the first four months of FY 2005 have been stronger than expected.

Other sources that are expected to decrease include financial institutions privilege tax receipts and liquor drink tax receipts. The liquor drink receipts were revised downward by \$200,000, while financial institutions income tax receipts were revised downward by \$12.5 million. It is not evident why this source has dropped dramatically. However, the Department of Revenue is investigating the possible causes.

FY 2006. Total State General Fund receipts are estimated to be \$4.84 billion in FY 2006, while tax receipts are estimated to be \$4.68 billion. The total receipts are \$210.0 million, or 4.5 percent greater than the newly revised FY 2005 figure. Tax receipts only for FY 2006 are estimated to increase \$138.0 million, or 3.0 percent.

The FY 2006 estimate does not subtract any demand transfers converted to revenue transfers, while the FY 2005 estimate subtracts \$71.8 million in demand transfers that were converted to revenue transfers. If transfers are treated in a similar fashion in both years, the FY 2006 growth would be \$138.2 million, or 2.9 percent. Modest increases are forecast for the principal State General Fund tax revenue sources in FY 2006 over the FY 2005 levels.

Accuracy of Consensus Revenue Estimates

For 30 years, State General Fund revenue estimates for Kansas have been developed using the consensus revenue estimating process. Besides the three state agencies identified on the first page, the economists currently involved in the process are Joe Sicilian from the University of Kansas, Ed Olson from Kansas State University, and John Wong from Wichita State University. Each of those involved in the process prepared independent estimates and met on November 3, 2004, to discuss estimates and come to a consensus for each fiscal year.

The table on page 7 presents estimates compared to actual receipts since FY 1975, the fiscal year for which the current process was initiated. The process involves comparing the adjusted original estimate to actual collections and then the final estimate is compared to actual receipts.

Concluding Comments

Consensus revenue estimates are based on current federal and state laws and their current interpretation. The group will meet again in April to revise these estimates. Developments which occur between the November and April meetings will be taken into account at that time.

ACCURACY OF STATE GENERAL FUND ESTIMATES

Fiscal Year	Adjusted Original Estimate*	Adjusted Final Estimate**	Actual Receipts	Difference from:			
				<u>Original Estimate</u>	<u>Final Estimate</u>	<u>Original Estimate</u>	<u>Final Estimate</u>
				Amount	Percent	Amount	Percent
1975	\$ --	\$ 614.9	\$ 627.6	\$ --	-- %	\$ 12.7	2.1 %
1976	676.3	699.7	701.2	24.9	3.7	1.4	0.2
1977	760.2	760.7	776.5	16.3	2.1	15.8	2.1
1978	830.1	861.2	854.6	24.5	3.0	(6.5)	(0.8)
1979	945.2	1,019.3	1,006.8	61.6	6.5	(12.5)	(1.2)
1980	1,019.3	1,095.9	1,097.8	78.5	7.7	1.9	0.2
1981	1,197.1	1,226.4	1,226.5	29.4	2.5	0.1	--
1982	1,351.3	1,320.0	1,273.0	(78.3)	(5.8)	(47.0)	(3.6)
1983	1,599.2	1,366.9	1,363.6	(235.6)	(14.7)	(3.2)	(0.2)
1984	1,596.7	1,539.0	1,546.9	(49.8)	(3.1)	7.9	0.5
1985	1,697.7	1,679.7	1,658.5	(39.2)	(2.3)	(21.3)	(1.3)
1986	1,731.2	1,666.4	1,641.4	(89.8)	(5.2)	(25.0)	(1.5)
1987	1,903.1	1,764.7	1,778.5	(124.6)	(6.5)	13.8	0.8
1988	1,960.0	2,031.5	2,113.1	153.1	7.8	81.6	4.0
1989	2,007.8	2,206.9	2,228.3	220.5	11.0	21.4	1.0
1990	2,241.2	2,283.3	2,300.5	59.3	2.6	17.2	0.8
1991	2,338.8	2,360.6	2,382.3	43.5	1.9	21.7	0.9
1992	2,478.7	2,454.5	2,465.8	(12.9)	(0.5)	11.3	0.5
1993	2,913.4	2,929.6	2,932.0	18.6	0.6	2.4	0.1
1994	3,040.1	3,126.8	3,175.7	135.6	4.5	48.9	1.6
1995	3,174.4	3,243.9	3,218.8	44.4	1.4	(25.1)	(0.8)
1996	3,428.0	3,409.2	3,448.3	20.3	0.6	39.0	1.1
1997	3,524.8	3,642.4	3,683.8	159.0	4.5	41.4	1.1
1998	3,714.4	3,971.0	4,023.7	309.3	8.3	52.7	1.3
1999	3,844.7	4,051.9	3,978.4	133.7	3.5	(73.4)	(1.8)
2000	4,204.1	4,161.0	4,203.1	(1.0)	--	42.1	1.0
2001	4,420.7	4,408.7	4,415.0	(5.7)	(0.1)	6.4	0.1
2002	4,595.8	4,320.6	4,108.7	(565.6)	(12.1)	(211.7)	(4.9)
2003	4,641.0	4,235.6	4,245.6	(395.4)	(9.3)	9.9	0.2
2004	4,605.5	4,450.0	4,518.7	(56.8)	(1.9)	68.2	1.5

* The adjusted original estimate is the estimate made in November or December prior to the start of the next fiscal year in July and adjusted to account for legislation enacted, if any, which affected receipts to the SGF.

** The final estimate made in March or April is the adjusted original estimate plus or minus changes subsequently made by the Consensus Estimating Group. It also includes the estimated impact of legislation on receipts.

Table 1
Consensus Resources Estimates for Fiscal Years 2005 & 2006
and FY 2004 Actual Receipts
(Dollars in Thousands)

	FY 2004 (Actual)		FY 2005 (Revised)		FY 2006	
	Amount	Percent Change	Amount	Percent Change	Amount	Percent Change
Property Tax:						
Motor Carrier	\$19,497	24.0 %	\$21,000	7.7 %	\$22,000	4.8 %
Motor Vehicle	\$185	n/app	800	n/app		
Ad Valorem	\$15,258	n/app	1,100	n/app		
Total	\$34,940	122.1 %	\$22,900	(34.5) %	\$22,000	(3.9) %
Income Taxes:						
Individual	\$1,888,434	7.9 %	\$1,960,000	3.8 %	\$2,060,000	5.1 %
Corporation	141,173	34.2	152,000	7.7	155,000	2.0
Financial Inst.	25,435	(18.3)	22,000	(13.5)	22,000	--
Total	\$2,055,042	8.9 %	\$2,134,000	3.8 %	\$2,237,000	4.8 %
Estate Tax	\$48,063	2.4 %	\$50,000	4.0 %	\$51,000	2.0 %
Excise Taxes:						
Retail Sales	\$1,612,067	2.8 %	\$1,650,000	2.4 %	\$1,700,000	3.0 %
Compensating Use	214,502	(5.1)	233,000	8.6	237,000	1.7
Cigarette	119,787	(7.3)	118,000	(1.5)	117,000	(0.8)
Tobacco Products	4,796	6.3	5,000	4.3	5,200	4.0
Cereal Malt Bev.	2,165	(4.8)	2,200	1.6	2,100	(4.5)
Liquor Gallonage	15,843	7.0	16,000	1.0	16,000	--
Liquor Enforcement	40,257	3.7	43,000	6.8	45,000	4.7
Liquor Drink	7,153	4.5	7,500	4.9	7,700	2.7
Corp. Franchise	36,805	18.4	48,000	30.4	45,000	(6.3)
Severance	84,641	16.3	105,400	24.5	88,000	(16.5)
Gas	66,055	17.4	79,100	19.7	66,300	(16.2)
Oil	18,586	12.5	26,300	41.5	21,700	(17.5)
Total	\$2,138,016	2.1 %	\$2,228,100	4.2 %	\$2,263,000	1.6 %
Other Taxes:						
Insurance Prem.	\$107,603	13.9 %	\$100,000	(7.1) %	\$100,000	-- %
Miscellaneous	3,646	(17.6)	4,500	23.4	4,500	--
Total	\$111,249	12.5 %	\$104,500	(6.1) %	\$104,500	-- %
Total Taxes	\$4,387,310	5.9 %	\$4,539,500	3.5 %	\$4,677,500	3.0 %
Other Revenues:						
Interest	\$13,870	(27.3) %	\$25,100	81.0 %	\$40,350	60.8 %
Net Transfers	16,718	(228.2)	(2,700)	(116.2)	65,800	n/app
Demand to Revenue	(62,699)	n/app	(71,800)	n/app	--	(100.0)
Other Transfers	79,417	n/app	69,100	n/app	65,800	(4.8)
Agency Earnings	55,290	6.8	69,000	24.8	57,200	(17.1)
Federal Grants	45,710	n/app	--	n/app	--	n/app
Total	\$131,588	27.0 %	\$91,400	(30.5) %	\$163,350	42.0 %
Total Receipts	\$4,518,898	6.4 %	\$4,630,900	2.5 %	\$4,840,850	4.5 %

Table 2
State General Fund Receipts
FY 2005 Revised
Comparison of November 2004 Estimate to April 2004 Estimate As Adjusted for Legislation
(Dollars in Thousands)

	FY 2005 CRE Est. As Adjusted for Legislation after 04/20/04	FY 2005 CRE Est. Revised 11/03/04	Difference	
			Amount	Pct. Chg.
Property Tax:				
Motor Carrier	\$19,500	\$ 21,000	\$1,500	7.7 %
Motor Vehicle	400	800	400	n/app
Ad Valorem	1,000	1,100	100	n/app
Total	\$20,900	\$ 22,000	\$1,100	5.3 %
Income Taxes:				
Individual	\$1,899,904	\$ 1,960,000	\$60,096	3.2 %
Corporation	130,000	152,000	22,000	16.9
Financial Inst.	34,500	22,000	(12,500)	(36.2)
Total	\$2,064,404	\$ 2,134,000	\$69,596	3.4 %
Estate Tax	\$49,000	\$ 50,000	\$1,000	2.0 %
Excise Taxes:				
Retail Sales	\$1,670,941	\$ 1,650,000	(20,941)	(1.3) %
Compensating Use	224,290	233,000	8,710	3.9
Cigarette	118,000	118,000	--	--
Tobacco Product	4,900	5,000	100	2.0
Cereal Malt Beverage	2,200	2,200	--	--
Liquor Gallonage	16,000	16,000	--	--
Liquor Enforcement	42,000	43,000	1,000	2.4
Liquor Drink	7,700	7,500	(200)	(2.6)
Corporate Franchise	42,300	48,000	5,700	13.5
Severance	77,600	105,400	27,800	35.8
Gas	58,900	79,100	20,200	34.3
Oil	18,700	26,300	7,600	40.6
Total	\$2,205,931	\$ 2,228,100	\$22,169	1.0 %
Other Taxes:				
Insurance Premium	\$100,000	\$ 100,000	\$ --	-- %
Miscellaneous	4,500	4,500	--	--
Total	\$104,500	\$ 104,500	\$ --	-- %
Total Taxes	\$4,444,735	\$ 4,539,500	\$94,765	2.1 %
Other Revenues:				
Interest	\$21,500	\$ 25,100	\$3,600	16.7 %
Net Transfers	11,530	(2,700)	(14,230)	n/app
Demand to Revenue Transfers	(74,600)	(71,800)	2,800	n/app
Other Transfers	86,130	69,100	(17,030)	(19.8)
Agency Earnings	63,956	69,000	5,044	7.9
Federal Grants	--	--	--	--
Total Other Revenue	\$96,986	\$ 91,400	(\$5,586)	(5.8) %
Total Receipts	\$4,541,721	\$ 4,630,900	\$89,179	2.0 %

Table 3
State General Fund Receipts
FY 2006
Comparison of Revised FY 2005 CRE Estimate to Initial FY 2006 Estimate
(Dollars in Thousands)

			Difference	
	FY 2005 CRE Est. Revised 11/03/04	FY 2006 CRE Est. 11/03/04	Amount	Pct. Chg.
Property Tax:				
Motor Carrier	\$21,000	\$ 22,000	\$1,000	4.8 %
Motor Vehicle	800	--	(800)	n/app
Ad Valorem	1,100	--	(1,100)	n/app
Total	\$22,900	\$ 22,000	(\$900)	(3.9)
Income Taxes:				
Individual	\$1,960,000	\$ 2,060,000	\$100,000	5.1 %
Corporation	152,000	155,000	3,000	2.0
Financial Inst.	22,000	22,000	--	--
Total	\$2,134,000	\$ 2,237,000	\$103,000	4.8 %
Estate Tax	\$50,000	\$ 51,000	\$1,000	2.0 %
Excise Taxes:				
Retail Sales	\$1,650,000	\$ 1,700,000	50,000)	3.0 %
Compensating Use	233,000	237,000	4,000	1.7
Cigarette	118,000	117,000	(1,000)	(0.8)
Tobacco Product	5,000	5,200	200	4.0
Cereal Malt Beverage	2,200	2,100	(100)	(4.5)
Liquor Gallonage	16,000	16,000	--	--
Liquor Enforcement	43,000	45,000	2,000	4.7
Liquor Drink	7,500	7,700	200	2.7
Corporate Franchise	48,000	45,000	(3,000)	(6.3)
Severance	105,400	88,000	(17,400)	(16.5)
Gas	79,100	66,300	(12,800)	(16.2)
Oil	26,300	21,700	(4,600)	(17.5)
Total	\$2,228,100	\$ 2,263,000	\$34,900	1.6 %
Other Taxes:				
Insurance Premium	\$100,000	\$ 100,000	\$ --	-- %
Miscellaneous	4,500	4,500	--	--
Total	\$104,500	\$ 104,500	\$ --	-- %
Total Taxes	\$4,539,500	\$ 4,677,500	\$138,000	3.0 %
Other Revenues:				
Interest	\$25,100	\$ 40,350	\$15,250	60.8 %
Net Transfers	(2,700)	65,800	68,500	n/app
Demand to Revenue Transfers	(71,800)	--	71,800	(100.0)
Other Transfers	69,100	65,800	(3,300)	(4.8)
Agency Earnings	69,000	57,200	(11,800)	(17.1)
Federal Grants	--	--	--	--
Total Other Revenue	\$91,400	\$ 163,350	\$71,950	78.7 %
Total Receipts	\$4,630,900	\$ 4,840,850	\$209,950	4.5 %